IN THE

Supreme Court of the United States

October Term, 1968

No. 1279

UNITED STATES OF AMERICA, Petitioner

v.

IDEAL BASIC INDUSTRIES, INC.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

RESPONSE TO THE PETITION FOR REHEARING

The Government bases its Petition for Rehearing on the decision rendered by the Court of Appeals for the Ninth Circuit in *United States* v. *California Portland Cement Company,* 413 F.2d 161, handed down on June 4, 1969 (two days after a writ of certiorari was denied in the instant case), alleging disagreement between the Ninth Circuit opinion and that of the Tenth Circuit with respect to the treatment in the proportionate profits computation of two expense items. One of these items, selling expenses, was treated by the Ninth Circuit contrary to the Government's position. It is noteworthy that the Government has not seen fit to file a petition for certiorari in the Ninth Circuit case.[1]

[1] The Ninth Circuit denied a petition for rehearing in the California Portland Cement case on July 1, 1969 (413 F.2d 161), and neither the Government nor the taxpayer has petitioned this Court for certiorari.

We respectfully submit that the Government's petition for rehearing provides no substantial basis for vacating the order denying its petition for certiorari, or for granting the writ. The alleged conflict in legal principles does not exist, and the most that can be said is that there is a difference between the Ninth Circuit and the Tenth Circuit in respect of the latter's essentially factual determination that cement in bulk was the first marketable product. The resulting difference in treatment of bags and bagging expense presents no important question of law, the issue being a minor accounting detail in the proportionate profits computation, without any significant effect on the revenues.

1. **Selling Expenses.** The Government strongly implies that there is a difference between the Ninth and Tenth Circuit decisions in the amount of the taxpayer's allowable depletion deduction, resulting from a difference in their treatment of selling expenses. Such a contention would be patently erroneous. While the court below in this case excluded selling expenses entirely from the proportionate profits computation, the mathematical effect of this treatment is the same—as the Government itself recognized in its reply brief, page 3—as the ratable allocation of those expenses between mining and nonmining. The Government there stated that the Tenth Circuit: "has, in effect, allocated them ratably between the mining and nonmining phases of the operation" (see, also, its original petition for certiorari, p. 6). This is precisely the treatment accorded selling expenses by the Ninth Circuit in the *California Portland Cement* case, wherein the Court stated, contrary to the Government's position in that case and in this case: "We further hold that the selling expenses in the instant case are to be allocated in the proportion that the mining costs bear to the total cost" (p. 172). There is not present here a conflict on any important question of law, nor is there any difference in tax effect;

there is merely a difference in the arithmetical method of arriving at the same result.[2]

2. **Bags and Bagging.** The treatment of the bags and bagging expense turned on whether the first marketable product obtained from the mineral was bulk cement or merely cement, whether in bulk or in bags. This narrow point affects the determination of the representative market price, and hence, the gross sales which are to be used in the proportionate profits computation.[3] The Tenth Circuit held that bulk cement was in fact marketable and that there was no earlier point where the goods in process could be sold. It excluded from the representative market price and from gross sales the extra amount received from customers for cement shipped in bags (the so-called "bag premium"). The related bagging costs were similarly excluded from the computation. Under the Ninth Circuit's decision, the bag premium must be added to the gross sales and the related bagging costs must be taken into account in the cost ratio. It will be entirely fortuitous in an individual case, depending on the relative profit on sales of cement shipped in bags compared with sales of bulk cement, whether the Tenth Circuit or the Ninth Circuit method is adverse to the revenues. In any event, this essentially factual point does not involve any important principle of law which warrants review by this Court.

3. **Additives.** No comment need be made on the third question presented—the treatment of the costs of grinding and blending additives into the kiln feed—since admittedly,

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[2] See appendix hereto.

[3] There is no dispute in this case as to the proper cutoff point for the determination of the taxpayer's "gross income from mining." As pointed out on page 4 of the Petition for Certiorari, the cutoff point was fixed by statute, and by the taxpayer's timely election, at the point where the ground and blended raw materials were fed into rotary kilns (Pub.L. 86-564, 74 Stat. 290; Pub.L. 86-781, 74 Stat. 1017; I.R.C. 1954, § 613(c)(4)(F)).

this item is not involved in the *California Portland Cement* case, as the Government concedes (Petition for Rehearing, p. 3).

For the reasons stated in the Brief for Respondent in Opposition and those stated herein, we urge that the Petition for Rehearing be denied.

Respectfully submitted,

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APPENDIX

The purpose of this appendix is to demonstrate that the treatment of selling expenses in the proportionate profits computation by the Ninth Circuit in the *California Portland* case and by the Tenth Circuit in the *Ideal Basic Industries* case produces the identical gross income from mining and hence the identical tax effect, even though different arithmetical methods are used to arrive at the same result.

Assumptions

Cement sales		$1,000
Mining costs	$200	
Nonmining Costs (not including selling)	600	
Total Costs (not including selling)	$800	
Selling expense	100	900
Net Profit		$ 100

Ninth Circuit[1]

$$\frac{\text{Mining Costs } (\$200)}{\text{Total Cost } (\$800)} \times \text{Selling Expenses } (\$100) = \$25 \text{ allocable to mining}$$

$$\frac{\text{Mining Costs } (\$200) + \text{Allocable Selling Expense } (\$25)}{\text{Total Cost } (\$800) + \text{Total Selling Expense } (\$100)}$$

$$= \frac{\$225}{\$900} = \text{Mining Costs/Total Cost Ratio} = 25\%$$

Gross Income From Mining: 25% × Sales ($1,000) = $250

[1]Selling expenses are "to be allocated in the proportion that the mining costs bear to the total cost . . . . " (413 F.2d, p. 172)

Tenth Circuit[2]

$$\frac{\text{Mining Costs } (\$200)}{\text{Total Cost } (\$800)} = \text{Mining Costs/Total Cost Ratio} = 25\%$$

Gross Income From Mining: 25% × Sales ($1,000) = $250

[2]"[S]elling costs are not a proper part of the computation." (404 F.2d, p. 126)